

DEPARTMENT OF FINANCE
ROOM RENTAL TAX COLLECTIONS
MAY 2000

May 2000

The County Council and County Executive
of Howard County, Maryland

Pursuant to Section 212 of the Howard County Charter and Council Resolution 22-1985, we
have conducted a review of selected activities of the

DEPARTMENT OF FINANCE
ROOM RENTAL TAX COLLECTIONS

and our report is submitted herewith. The scope of our examination related specifically to a follow-up review of the recommendations made in our March 1995 report and a review of current operations. The body of our report presents our findings and recommendations.

The contents of this report have been reviewed with the Chief Administrative Officer and the Director of Finance. We wish to express our gratitude to the Department of Finance employees for the cooperation and assistance extended to us during the course of this engagement.

Ronald S. Weinstein, C.P.A.
County Auditor

Stephanie Glaros, C.P.A.
Auditor-in-Charge

DIGEST

In August 1992, Howard County, in accordance with section 20.451 of the Howard County Code, began imposing a room rental tax of 5% at hotels and motels located in the County. This tax is imposed on revenues collected from guests staying less than 30 consecutive days and whose charges are not paid through a tax exempt agency. The room rental taxes that were collected during the prior month must be paid to the County on or before the last day of each month. To ensure that the proper amount of tax was being collected in accordance with County laws, we performed an audit of these revenues in March of 1995. That audit involved visiting ten of the thirty hotels or motels in the County or their accountants and issuing a report which contained eight recommendations to improve the tax collection process. We have now completed a follow-up of that report to determine the current status of the original eight recommendations and to test additional facilities. We found that two of the original recommendations which relate to hotel/motel record keeping have not been implemented. We have included these recommendations in our current report because we believe that they still need to be implemented.

As part of our continuing review of the rental tax collection process, we examined the records of ten additional hotels or motels for adherence to County tax laws. Several were found to maintain inadequate records relating to this tax. In several instances, exemptions were improperly taken and/or not documented. Two motels did not maintain source documentation or any other record as to what the exemptions pertained to. We have recommended that the Department of Finance make all hotels and motels aware of the County laws relating to the room rental tax and of the records required to document the exemptions taken. Civil penalties can be imposed for failure to provide required information and/or maintain sufficient records supporting the room rental charges and the amount of taxes collected. Penalties and interest may also be assessed on late payments and failure to make payment. We have also recommended that the Department of Finance send an invoice to one specific motel for additional taxes due because it could not show tax exempt status. In another instance, the motel records could not be reconciled to the tax reports submitted to the County by the motel. We reviewed this information with the State's Attorney Office and concluded the violations were not material or criminal and, therefore, did not warrant further investigation. We have also recommended that the Department of Finance inform hotel/motel owners that exemptions must have proper documentation or the exemption will be disallowed.

INTRODUCTION AND SCOPE

In March 1995, the Office of the County Auditor issued a report on the room rental tax collection process. The scope of that audit related specifically to a review of the records of ten hotels or motels in Howard County and their adherence to County room rental tax laws. As part of our audit process, we perform follow-up reviews on completed audits to determine the current status of the original report recommendations and to review existing operations. We have also reviewed the records of ten additional hotels or motels as they relate to the collection and payment to Howard County of the room rental tax.

At each location, we reviewed two types of information, where available: 1) Tax returns or audited financial statements to compare the annual revenue on these documents to the annual revenue shown on the room rental tax reports. 2) Daily room rental cards to compare to the daily entries on the monthly recap sheets which were then compared to the monthly room rental tax reports. Our conclusions were based on a review of these documents.

FOLLOW-UP OF RECOMMENDATIONS

We performed an audit of the hotel and motel room rental tax and issued a report in March 1995. That audit involved examining the room rental tax collection process at ten of the hotels or motels in the County. The contents of that report included eight recommendations for the areas that we felt needed improvement. The scope of this follow-up included examining the status of the implementation of those recommendations. In December 1999, the Director of Finance sent a letter to all hotel/motels in the County informing them of specific reporting requirements. This satisfied two of the eight recommendations. The other four recommendations were implemented prior to the beginning of our fieldwork. The two remaining recommendations have not been implemented.

Recommendations in the 1995 report that have not been implemented are as follows:

1. *The Department of Finance review each tax remittance form for accuracy and completeness.*

Current Status:

In our current review we found two motels that were not completing all sections of the tax remittance form. We recommend the review process include all parts of the form.

Administration's Response:

The Administration concurs with this recommendation. Written procedures will be drafted by the Department of Finance to ensure verification of accuracy and completeness for all submitted tax remittance forms. Currently each month forms are reviewed and if the report is incomplete or errors exist, the hotel/motel operator receives written notification of the problem. The Department of Finance performs a follow up for all outstanding reports in a timely manner. The Department of Finance is planning to create a database to account for all hotel/motels doing business in the County to ensure compliance.

2. *The organizations providing emergency housing give each person using this service some form of documented authorization to be kept by the hotel or motel to validate the tax exempt status.*

Current Status:

In FY 1995, the Administration responded that this was unnecessary because of registers to be kept by hotels/motels. However, no registers of exempt income were found. In December 1999, the Department of Finance sent all hotel/motel owners a sample register of exempt income to be maintained on a monthly basis. Furthermore, effective July 1, 2000, the Department of Finance will require all agencies approved for emergency housing certificates

to provide the Department of Finance with a monthly report which includes the name of the hotel/motel, the dates of stay and the room rent charged.

Administration's Response:

The Administration concurs with this recommendation. Effective July 1, 2000, the Department of Finance will require all agencies approved for emergency housing certificates to provide the Department of Finance with monthly statistical reports. These reports will include the hotel, dates of stay and the room rent charged.

CURRENT FINDINGS

We examined ten additional hotels or motels for adherence to County room rental tax laws. At several locations, we discovered that the exemptions were not properly taken and/or properly documented. We have included eight new recommendations which relate to the determination and documentation of the exemptions.

At one of the hotels, we found only a summary sheet to support the exemption amounts. The hotel did not maintain source documentation or any other records to explain the exemptions. At the end of a guest's stay, if they are entitled to an exemption, the clerk prepares an adjustment sheet to remove the tax. At the end of the month, a summary of all adjustments is prepared. The exempt income is computed by dividing the total adjustments made to local tax by 5%, the Howard County tax rate. The documentation provided to us was not adequate to verify the accuracy of the exemption amount. In order to insure that the hotels document their exemptions, we again recommend that:

1. **The Department of Finance notify hotel/motel owners that undocumented exemptions will be disallowed.**

Administration's Response:

The Administration concurs with this recommendation. The Department of Finance is planning to send a follow-up letter prior to July 2000 to hotel/motel establishments addressing the "Exempt" status, i.e., qualification and statistics from the emergency housing agencies.

_____ We found that one motel was giving many guests tax exemptions to which they were not entitled. We reviewed the register of rooms rented for a four-month period. This register listed the room rented, the guest's name, if the guest was staying over another night, the room rental rate and the state and local tax. We noted 23 customers who, according to the register, were not charged tax and had not stayed 30 or more consecutive days. We asked the motel owner for an explanation of why the guests were not charged tax and he said that he could not prove that the guests should be exempt and he requested that we send him a bill for taxes due. We informed him of the exemption rules. For the four-month period, exempt income was over-reported by approximately \$9,800. Over a 12-month period, this would amount to approximately \$29,400 in income or an understatement of \$1,470 in County tax. We recommend that:

2. *The Department of Finance send a bill to the motel for additional taxes due in the amount of \$1,470.*

Administration's Response:

The Administration concurs with this recommendation. The Department of Finance has requested information from the Auditors to invoice the responsible party.

3. *The Department of Finance inform all hotel/motels of the County laws/requirements regarding exemptions.*

Administration's Response:

The Administration concurs with this recommendation. The Department of Finance has completed the revised form and a letter of explanation will be sent to all hotel/motel owners. This follow-up letter will be more specific in addressing the exemptions and how the department will verify the exemptions reported. Also, the Department of Finance will address the length of stay for exemption to be 30 days instead of the 25 days.

In the 1995 report, we recommended that the County Administration look into revising the law to make it more consistent with State law. The State law exempted room tax after 30 days while the County law exempted tax after 25 days. In 1998, this recommendation was implemented with a change to the County law (Council Bill 38-1998) which changed the length of stay for an exemption from 25 to 30 days. This made the exemption requirement the same for both the County and the State. However, during our review, we noted that the correspondence with the hotels/motels and some of the records at the hotels/motels still reflected the old law which state that visits over 25 days are exempt. We recommend that:

4. *The Department of Finance inform all hotels/motels in writing that the length of stay required for exemptions is 30 days.*

Administration's Response:

The Administration concurs with this recommendation.

_____At another hotel we found that tax exemptions were not properly administered. The hotel was giving the exemption starting at the end of the exemption period while the guest should be exempt for their entire stay if it is more than 30 consecutive days. If the guest makes a request for a refund,

the hotel will reimburse the guest. At that time, an adjustment would be made to the general ledger and they would reduce the tax payable to the County. To ensure that hotels are properly collecting tax, we recommend that:

5. **The Department of Finance again notify the hotels and motels on how to implement the County law relating to length of stay for exemptions.**

Administration's Response:

The Administration concurs with this recommendation.

_____ This hotel was also failing to properly report exempt income. It was taking what it considered to be net income subject to Howard County room rental tax and reporting that as gross income. This results in the gross income, the amount of exemptions and the occupancy rate of the hotel being understated. Although the County tax remained the same, we made the accountant aware of the situation and she indicated that the form would be filled out correctly in the future. We recommend that:

6. **The Department of Finance inform all hotel and motel owners that gross income should include exempt income which should then be subtracted to arrive at taxable income.**

Administration's Response:

The Administration concurs with this recommendation. The follow-up letter as stated in #3 will explain gross income, exempt income, and taxable income.

During our examination, a motel employee provided us with information which indicated that the monthly tax sheets sent to the County did not agree with the actual revenue of that motel. Although this employee gave us a separate set of summary records, we were unable to verify the County tax filings to the organization's books. The hotel was also missing documentation to support the exemptions. While our audit was in progress there was a change in management. We expanded our audit of this hotel to include two months of calendar year 1999. In reviewing these two months, we were not able to agree the gross revenue and tax exempt income reported to the County to the organization's records although we were able to verify the County tax. We discussed this matter with

the State's Attorney and concluded that it was not criminal in nature and not material and, therefore, did not warrant further investigation. We recommend that:

7. *All organizations that provide emergency housing prepare a monthly report for the County that includes the name of the hotel/motel, the dates of stay and the room rent charged.*

Administration's Response:

The Administration concurs with this recommendation. The Department of Finance will send a letter to all agencies holding Emergency Housing Certificates. This letter will be sent before July 2000 advising of the new reporting requirement.

8. *Periodic review of exempt income be performed to ensure that proper documentation is being maintained.*

Administration's Response:

The Administration concurs with this recommendation. As part of the review process of the tax reports, the Department of Finance will verify the exempt income as reported from the agencies with Emergency Housing Certificates.

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